THE COMMONWEALTH OF MASSACHUSETTS

DEPARTMENT OF TELECOMMUNICATIONS & ENERGY

ONE SOUTH STATION

BOSTON, MA 02110
(617) 305-3500

July 6, 2006

Gary L. Beland
New England Gas Company
100 Weybosset Street
Providence, RI 02903

RE: Petition of New England Gas Company for approval of proposed changes to its gas procurement practices, D.T.E. 06-3.

Dear Mr. Beland:

On January 3, 2006, New England Gas Company ("New England" or "Company") filed a letter with the Department of Telecommunications and Energy ("Department") in which the Company requested Department authorization to implement a change in its gas purchasing practices designed to mitigate price volatility for its customers ("Company Letter"). On January 24, 2006, the Department issued a Notice for Comments. KeySpan Energy Delivery New England ("KeySpan") filed comments on February 17, 2006, and the Office of the Attorney General ("Attorney General") filed comments on February 21, 2006.

Company's Proposal

In the Company Letter, New England states that currently it purchases approximately 28 percent of the gas volumes needed to meet peak-season customer requirements in roughly equal increments over a seven-month period from April through October, and these volumes are stored (Company Letter at 1). The Company also states that the remainder of its gas supply needed to meet peak-season customer requirements is purchased at the time that the gas will be consumed based on "first-of-the-month" and "spot," or daily market pricing, both of which are generally based on published index prices (id.). New England asserts that these prices are susceptible to market volatility and short-term speculation, and, therefore, have the potential to drive price changes in the Company's gas adjustment factor ("GAF") (id.). The

Company further states that in recent years, natural gas prices have tended to increase sharply but decrease at a much more gradual rate (id. at 2).

Therefore, the Company proposes to purchase up to one-half of its non-storage, annual gas-supply purchase requirements over a 20-month period commencing after the Department's approval of the Company's proposal (id.). The Company proposes to use this mitigation strategy for both the peak and off-peak periods, because recent experience has shown that both winter and summer months are now subject to substantial price volatility(id. at 3). The Company notes that, by locking in prices for both seasons, the percentage of gas costs stabilized rises from 50 percent of total deliveries to approximately 65 percent (id.). The Company proposes to implement the plan by locking in the New York Mercantile Exchange ("NYMEX") portion of gas commodity prices with suppliers serving the Company (id. at 2-3). The Company would implement an expanded proportion of locked-in purchases for earlier months in order to achieve the benefits of the plan on an expedited basis (id. at 3).

New England asserts that stabilization of prices will also benefit transportation customers (id.). The Company asserts that a reduction in the frequency and magnitude of rate changes will help transportation customers evaluate transportation service as an alternative, by providing a more accurate and consistent price for comparison shopping (id.). Finally, New England contends that the proposal would provide a more accurate and consistent price signal for investments in conservation because the prices are indicative of long-term trends rather than short-term volatility (id.).

Comments

KeySpan supports the Company's proposal, noting favorable results of its own price volatility mitigation plan, as well as New England's similar experience in Rhode Island (KeySpan Comments at 1-2). In his comments, the Attorney General supports the Company's effort to mitigate price volatility and states that the Department should approve the Company's proposal if the Department determines that the proposal benefits consumers by mitigating volatility in natural gas prices (Attorney General's Comments at 2). Nonetheless, the Attorney General recommends that the Department require the Company to track the costs that the Company would have paid under the current procurement program and the actual costs paid under the forward procurement plan (id.).

Analysis and Findings

The Department's standard of review requires that a local gas distribution company ("LDC") show that a risk management plan is reasonably designed to meet the objective of price stability. D.T.E. 01-100-A at 28. Before the Department will approve any risk management plan, said plan must meet six requirements. The first requirement is that customers be allowed to voluntarily participate in the program.[1] Id. We find that this directive is inapplicable because the Company's proposal does not involve a fixed-priced optional service for a subset of customers who are willing to pay a premium for that fixed price, therefore there is no danger of misallocation of costs.

The second requirement is that the plan maintain the goal of volatility mitigation and price stability rather than the objective of procuring prices below indices. D.T.E. 01-100-A at 28. Under its proposal, New England would lock in prices on non-storage volumes at a rate of one-twentieth of the required volumes per month (Company Letter at 3). The Company states that it will base its purchases on NYMEX futures prices available each month (id. at 2). Given this information, the Department finds that the proposed purchasing strategy will limit the exposure of the Company's ratepayers to steep fluctuations in price. Therefore, the proposal meets the Department's second criterion to mitigate price volatility.

The third requirement is that the plan ensure fair competition in the gas supply market. D.T.E. 01-100-A at 29. The Department has stated that a financial risk-management program will not adversely affect gas unbundling and customer choice if it: (1) provides all customers with an opportunity to obtain more stable prices and costs are allocated only to those who participate in the program; and (2) does not impede efficient competition among all suppliers. Id. at 17. First, all of the Company's customers would benefit from the proposal because gas price volatility would be mitigated. Second, regarding efficient competition among suppliers, the Department has stated that risk-management programs will not negatively affect gas unbundling and customer choice if the recovery of costs by the LDC does not affect the reliability and transparency of the rates charged by the LDC. Id. at 16. Under the Company's proposal, there are no transaction costs to be recovered, so there is no effect on the reliability and transparency of rates (Exh. DTE 1-3). Accordingly, the Department finds that the proposal does not impede fair competition in the gas supply market.

The fourth requirement is that the Company allocate all costs of the risk-management program to program participants only. Id. at 29. There are no implementation costs associated with the program, hence there are no costs to allocate (Exh. DTE 1-3). Therefore, the fourth requirement is inapplicable.

The fifth requirement is that the Company demonstrate the effect of the plan on the reliability and transparency of commodity price. D.T.E. 01-100-A at 29. The Company proposes to change its schedule for gas purchasing and not the pricing mechanism (Company

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[1] The Department has stated that voluntary participation in risk-management programs is necessary because, "the costs associated with such a program shall be recovered from only the customers who choose to participate in the program." D.T.E. 01-100-A at 16.

Letter at 2,4). Because the same pricing indices that are currently used will continue to be used in the future, there will be no effect on the reliability and transparency of commodity price. Thus, the proposal meets the fifth requirement.

Finally, the sixth requirement is that the proposal contain no incentive mechanism. D.T.E. 01-100-A, at 29. No incentive mechanism has been proposed; consequently, the Company's proposal meets the sixth requirement.

In his comments, the Attorney General, recommends that the Department order the Company to track the costs that the Company would have paid under the current procurement program and the actual costs paid under the proposed program (Attorney General Comments at 2). We find that such a comparison would be helpful to the Department in evaluating the efficacy of the proposed program. Therefore, the Company shall keep data necessary to compare prices under its old procurement procedure to those under its new procurement procedure, and shall report the results of such a comparison as part of its seasonal cost of gas adjustment clause ("CGAC") filings.[2]

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[2] As stated above on page three, the goal of the Company's proposal is to mitigate gas price volatility, rather than to achieve prices below indices. Therefore, in directing this comparative data gathering, we do so to permit post-hoc comparison, but do not suggest that a possibly unfavorable comparison might be a basis for cost recovery disallowance.

Accordingly, for the reasons outlined above, the Department finds that the Company has shown that the plan is reasonably designed to meet the objective of price stability. Therefore, the Department approves New England Gas Company's gas procurement and volatility mitigation plan. However, as part of its seasonal CGAC filings, the Company must include the following information for all purchases made as part of its volatility mitigation plan: the volumes, indices, contracted price, and delivery date.

By Order of the Department,

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Judith F. Judson, Chairman

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James Connelly, Commissioner

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W. Robert Keating, Commissioner

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Brian Paul Golden, Commissioner